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SENSITIVE
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TREASURY FOR DO/IDD AND OUSED/IMF
SECDEF FOR USDP/DSCA
PASS EXIM FOR CLAIMS -- MPAREDES
PASS USDA FOR CCC -- ALEUNG/WWILLER/JDOSTER
PASS USAID FOR CLAIMS -- WFULLER
PASS DOD FOR DSCS -- PBERG

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SUBJECT: PARIS CLUB - PARIS CLUB - APRIL 2008 TOUR D'HORIZON AND
NEGOTIATION WITH LIBERIA

¶1. (SBU) Summary: At the Paris Club's April 16-17 session, the U.S. and other creditors signed an accord with Liberia to begin interim debt relief under the enhanced Heavily Indebted Poor Countries (HIPC) initiative. During the Tour d'Horizon, France, Germany, and the U.S. reported on recent bilateral contacts with Argentina. Finance Secretary Secondini told the French that Argentina hopes to reach a settlement by the end of 2008, and the French believe that Argentina is preparing a formal proposal to the Paris Club. The Secretariat urged Brazil to implement the 2004 debt treatment for Iraq, and the Club discussed relations with the Central African Republic, Cote d'Ivoire, Serbia, Seychelles, and Togo. Despite opposition from the United States and Sweden and

concerns raised by several other creditors, France continued to push its "fragile states" proposal for the Paris Club to provide an unconditional debt deferral for low-income countries that are participating in Emergency Post-Conflict Assistance (EPCA) programs with the IMF. The Secretariat also reported on what it characterized as promising initial technical meetings with multiple Chinese government ministries involved in PRC aid and lending activities. Creditors also discussed preparation of a Paris Club annual report. End Summary.

Argentina

12. (SBU) France reported Argentine Finance Secretary Secondini met Paris Club Chairman Musca on the margins of the IMF-World Bank Spring Meetings and expressed Argentina's desire to reach a settlement with the Paris Club by the end of the year. France said that, contrary to press reports, Sarkozy and Fernandez de Kirchner did not discuss debt in their April 7 meeting in Paris. According to the Secretariat's account, Secondini did not specify terms. The Secretariat believes the GOA, knowing it cannot obtain a traditional

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Paris Club rescheduling without an IMF program, is working instead on a voluntary arrears clearance proposal. The U.S. reported that senior Treasury and State Department officials recently met with their Argentine counterparts and pressed them to make a serious offer to the Club. Germany said it also met with Argentina but did not raise Paris Club issues. Separately, the Secretariat summarized the results of the latest data call. As of March 1, 2008, Argentina owed the Paris Club \$7.92 billion (excluding the \$1 billion

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restructured Spanish loan), of which \$5.36 billion consisted of arrears and \$1.21 billion consisted of late interest. Japan, Norway, and Spain said they had received modest payments on debts contracted after the December 1983 cutoff date. The Netherlands said it may have also received some payments but would confirm. The Secretariat will update the data call to reflect these payments and

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questioned whether Argentina was paying certain creditors selectively, which could complicate efforts to reach a settlement. Final payments on debts rescheduled through previous Paris Club agreements are due by the end of 2008.

Central African Republic (CAR)

13. (SBU) The IMF said a significant share of CAR's external debt is owed to non-Paris Club creditors, some of which are considering litigation. The IMF warned that it will be challenging for CAR to secure financing assurances from creditors holding 80 percent of the debt -- a requirement for reaching HIPC Completion Point. (CAR barely reached the 70 percent threshold necessary for the IMF to provide interim debt relief at Decision Point.) The authorities have approached the African Development Bank for legal assistance. The Secretariat said it was important for the Paris Club to maintain pressure on non-Paris Club creditors. One possibility is to send letters to CAR's non-Paris Club creditors, similar to what the Paris Club did for Iraq. Several creditors, including the U.S., reported that they were close to concluding bilateral agreements to implement the Paris Club's December 2007 HIPC Decision Point debt treatment.

Cote d'Ivoire

14. (SBU) The IMF said if Cote d'Ivoire performs satisfactorily under its second Emergency Post-Conflict Assistance (EPCA) program, it could reach HIPC Decision Point and begin to benefit from interim debt relief at the same time a follow-on Poverty Reduction and Growth Facility (PRGF) program is approved. The government would like to reach Decision Point by the end of 2008. The IMF noted,

however, that Cote d'Ivoire's track record under its first EPCA was not encouraging; overall performance was uneven, with unproductive

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spending and delays in structural reforms. The Secretariat said it could begin to think about the terms of an eventual Paris Club treatment and approach the London Club to discuss comparable treatment as soon as a macroeconomic framework is in place. Preliminary contacts with the London Club suggest willingness to have a cooperative dialogue. The Secretariat indicated that debts contracted after the January 1983 cutoff date may have to be included in the debt treatment. The IMF said most of Cote d'Ivoire's private debt is owed to the London Club and repeated previous statements that the Fund is not aware of any Ivorian debt held by litigating creditors. Reconciliation of debt data is well advanced. The World Bank reported that recent arrears clearance operations enabled the Bank to provide \$35 million in budget support and reactivate \$104 million in undisbursed funds. In the coming months, there will be approval of \$122 million in grants to support emergency urban infrastructure, government and institution building, among other projects.

Iraq

15. (SBU) The Secretariat reported that Iraq's advisers had asked the Secretariat to write to Algeria and Morocco and urge them to provide comparable treatment. Creditors gave their consent. The Secretariat asked Brazil for an update on progress toward concluding

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a bilateral agreement with Iraq. Brazil's delegation stated that, although Brazil participated in the 2004 negotiations, the GOB did not sign the Agreed Minute for three reasons: (1) it did not agree with the terms of the treatment; (2) the majority of Iraq's creditors was not present at the Paris Club negotiations, and Brazil did not know how those creditors would react to the Paris Club agreement; and (3) there were other complicating factors, including legal issues, involving many actors in Brazil. The Brazilian representative promised that a response to the Secretariat's letter would be forthcoming, adding that Brazil had maintained an open dialogue with Iraq's advisers and was working internally to find a solution even though Iraq was a very complicated issue domestically.

The Secretariat pressed the issue, noting that the situation had changed significantly since 2004. No longer could Brazil cite concerns about the reaction of other creditors considering that many of Iraq's creditors have delivered comparable treatment. The

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Secretariat reiterated that the comparability of treatment principle

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applies to all non-Paris Club creditors and especially to a country like Brazil that has participated in so many Paris Club meetings.

16. (SBU) The UK asked whether there had been further discussions with Iraq's EU creditors. The Secretariat said it had initiated contacts with Poland and Greece, but there was nothing to report yet. The U.S. asked for an update on Iraq's discussions with China and India. The Secretariat said an agreement with India had been concluded, and prospects for an agreement with China were good. [Note: our understanding is that this assessment may be a bit simplified and overly optimistic.] Spain asked the IMF about prospects for the third-phase review of the Stand-by Arrangement (SBA) occurring no later than December 31, 2008. The IMF reported that a mid-June mission will review the SBA; if performance is satisfactory, the IMF Executive Board could discuss the review in August or September.

Liberia

¶7. (U) During the April 17 negotiation, Paris Club creditors provided Liberia a flow treatment on the Club's standard terms for HIPC's at Decision Point. The Paris Club's "Agreed Minute" with Liberia commits creditors to provide debt relief on the following terms, although several creditors will provide more generous relief:

-- cancellation of 67 percent of arrears on non-official development assistance (ODA) debts contracted before the January 1983 cutoff date and rescheduling the residual amount over 23 years, with a 6-year grace period,

-- rescheduling over 40 years (with a 16-year grace period) all pre-cutoff ODA arrears as well as all ODA debt service payments falling due during the three-year period of the IMF program, and

-- deferral of all post-cutoff date and short-term debt and to capitalize all moratorium interest payments, given Liberia's extremely limited capacity to pay.

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¶8. (U) As a result, a minimum of \$254 million of Liberia's \$1.4 billion Paris Club debt stock will be cancelled immediately, and Liberia will not have any payments due to the Paris Club during the period of the IMF program, as long as the program remains on track. Additional bilateral relief from the U.S. and other Paris Club creditors will further increase the amount of up-front cancellation.

Given the large proportion of arrears involved, this means the U.S. will cancel nearly \$400 million of Liberia's \$430 million debt to the U.S. when implementing the April 17 Paris Club accord. Liberia also committed to obtain comparable debt relief from its commercial and other bilateral creditors.

¶9. (SBU) Although HIPC Decision Point treatments are typically uncontroversial, two aspects of Liberia's request provoked debate. First, Liberia asked for zero payments during the period of the IMF program. The IMF's own balance of payments projections surprisingly showed that Liberia had the capacity to pay \$6 million to the Paris Club during the 2008-2010 program period, leading the Secretariat to suggest that Liberia apply the \$6 million to a small portion of moratorium interest on deferred post-cutoff date debt. Several creditors supported the Secretariat's proposal.

¶10. (SBU) The U.S. strongly disagreed, arguing that it was critical to provide Liberia a cushion given balance of payment risks, and citing the symbolic importance of zero payments. We reminded creditors of a recent precedent: when Haiti received its HIPC Decision Point treatment in December 2006, the Paris Club had not asked for any payments despite Haiti's larger capacity to pay. Germany strongly supported our position; Italy, Norway, and the UK also made helpful comments. The Secretariat did not try to defend its proposal and agreed that providing a cushion was important. A consensus quickly formed in favor of requiring zero payments.

¶11. (SBU) Liberia further asked the Paris Club to reduce pre-cutoff date non-ODA arrears by 90 percent rather than the standard 67 percent. Belgium, Germany, Italy, Norway, and the U.S. expressed their willingness to reduce these arrears by 90 percent; however, other creditors held to 67 percent. The Liberians did not insist, but rather asked creditors that intended to go beyond the terms of the Agreed Minute to publicize this additional debt relief through bilateral press releases.

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Serbia

¶12. (U) Switzerland said Serbia had declared that, even though the two countries had agreed on the text and figures of a bilateral agreement recognizing Serbia's share of the debt of the former Serbia and Montenegro, Serbia could not sign the bilateral agreement

until a new government takes office following May 11 elections. France said it was in the same position. The Secretariat promised to review the situation in May or June.

Seychelles

¶13. (SBU) The Seychellois finance minister told the Secretariat that the Seychelles intends to seek an IMF program, which it understands is a precondition for a Paris Club treatment. The IMF said the Seychellois principal secretary of finance met with Fund staff and also expressed interest in a program, although there has been no official written communication. The Secretariat expressed cautious optimism that the Seychelles is moving in the right direction. The government understands that comparability of treatment will require an approach to commercial creditors, and the Seychelles has also established a new debt committee in an attempt to exercise restraint on the central bank. (The U.S. is not a creditor.)

Togo

¶14. (U) The IMF said Togo's PRGF, which the Fund's Executive Board approved on April 21, could pave the way for debt relief under HIPC and the Multilateral Debt Relief Initiative (MDRI). Based on end-2007 data, Togo's high ratio of debt-to-government revenue is likely to exceed the 250 percent threshold necessary to qualify for HIPC. The preliminary HIPC document should be completed by late summer, and Togo could reach Decision Point if performance is strong when the IMF completes its first review of Togo's PRGF. The World Bank reported arrears to its International Development Association

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(IDA) and noted a May 29 Board discussion would address an arrears clearance operation similar to Cote d'Ivoire's, with actual arrears clearance to occur the following day. After budget support of \$18 million, there would be an IDA lending envelope. No date is set yet for clearance of arrears to the African Development Bank (AfDB), although preparations are well advanced. Germany said it received a letter from Togo asking for a 160,000 euros contribution toward the clearance of Togo's arrears to the African Development Bank. France explained that the AfDB will pay 99 percent of the arrears, leaving Togo to cover the remaining 1 percent -- an amount equal to 160,000 euros. Togo has also asked France to pay the 160,000 euros; discussions are ongoing. Assuming PRGF approval and arrears clearance to the World Bank and AfDB, negotiations in the Paris Club on a pre-HIPC debt treatment could take place in June. (U.S. claims total just \$6,000. We requested a de minimis clause at the March 2008 meeting.)

Methodological Discussion:
Fragile States

¶15. (SBU) Despite opposition from the U.S. and mixed reactions from other creditors, the Secretariat continued to press ahead with the proposal it first raised in March 2008 for the Paris Club to provide debt relief to low-income "IDA-only" countries, based on an IMF Emergency Post-Conflict Assistance (EPCA) program. (The proposal calls for the Paris Club, on a case-by-case basis, to defer all arrears and debt service falling due during the period of the EPCA, and to capitalize moratorium interest. If the country obtains a follow-on PRGF, creditors would reschedule deferred amounts and cancel the accrued moratorium interest.) The U.S. said it could not support the proposal. We reiterated our concerns about the precedent of providing debt relief -- even for a short period of time -- without conditionality and noted that the U.S. could face legal and budgetary obstacles in implementing such a deferral. The Secretariat did not appear overly concerned about potential U.S.

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legal difficulties, noting that the U.S. Congress had provided the

necessary legislation in the past in the context of the HIPC initiative.

¶16. (SBU) Creditors asked the Secretariat to 1) omit the reference PARIS 00000826 008 OF 010

to Iraq in the working paper (Russia); 2) insert a claw-back provision to strengthen the link to a PRGF (Spain); 3) await the result of IMF and IBRD deliberations on fragile states before acting (Netherlands); and 4) provide a list of countries that could receive such treatment (Italy).

¶17. (SBU) Germany argued against automatically providing a deferral and said it could not agree to defer all categories of debt, as the inclusion of post-cutoff-date debt could affect export credit agency cover policy. Germany, Japan, Sweden, and the UK all expressed concern about canceling moratorium interest without regard to the debtor country's capacity to pay once a PRGF is approved. Sweden seconded all these concerns, pointed out Sri Lanka was paying its debt when the tsunami occurred, and questioned whether the Secretariat's proposal was the right way to help fragile states.

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¶18. (SBU) No creditor other than the U.S. and Sweden, however, challenged the premise that the Paris Club should do something to help fragile states. (Despite its reservations, Sweden said it did not intend to block any Paris Club decision.) Indeed, several countries (Italy, Japan, Spain, UK) said they supported the proposal in principle. The Secretariat picked up on this sentiment, concluding that "no one" around the table disagreed that the Paris Club should try to help fragile states; the question was how to respond.

¶19. (SBU) Given creditors' desire to take into account the outcomes of IMF and IBRD discussions, the Secretariat said the previous U.S. proposal to send a letter stating the Club's willingness to provide a debt treatment once a PRGF is in place could serve as an initial step. The Secretariat offered to prepare a draft text for such a letter and update the working paper to reflect creditors' comments regarding conditionality. The Secretariat stressed that the deferral would be applied on a case-by-case basis rather than automatically to all IDA-only countries on EPCAs. Guinea-Bissau and the Comoros are likely candidates; Cote d'Ivoire and Lebanon are not. The Secretariat proposed that, as the results of IMF and IBRD meetings emerge, the Paris Club continue its "fragile states" discussion.

Methodological Discussion:

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Relationships with China

¶20. (SBU) Paris Club Secretary General Courbe reported on the Secretariat's March 31 visit to Beijing to discuss the practices of

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the Paris Club with PRC officials. The visit included separate meetings with staff-level officials from the Ministry of Commerce (MOFCOM), the Ministry of Foreign Affairs, and China Exim Bank. The four-hour MOFCOM meeting involved twenty officials, including Africa, external aid, research institute, MFA and central bank experts, a sign of interest in the dialogue. Commerce officials stressed that China's overseas aid was South-South cooperation and not comparable to development aid OECD countries provide; Commerce officials also strongly criticized conditionality attached to debt relief and development aid. Questions focused on the Paris Club's practices with respect to conditionality, debt swaps, and how exchange rates are handled in debt treatments. MFA officials made it clear that China could not become a member of the Paris Club, while at the same time acknowledging the Club's efforts in Africa. Exim Bank officials were also critical of conditionality but said

they were willing to share data and experiences concerning particular debtor countries. They also indicated a willingness to participate as an observer at a future Paris Club discussion; however, the Secretariat questioned whether China Exim's statement reflected a fully cleared position.

¶21. (SBU) The Secretariat was generally encouraged by these initial contacts. While it is clear that China is not prepared to associate itself in any formal way with the Paris Club, Chinese officials remain open to a technical dialogue. Possible next steps include inviting China's Ministry of Finance to discuss its own practices at a future Paris Club meeting; inviting China to participate in the Paris Club's annual meeting with the private sector, alongside other invited emerging market creditors; or inviting China to a seminar on debt not officially affiliated with the Paris Club. The Chinese have not responded to these ideas.

Methodological Discussion:
Paris Club Annual Report

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¶22. (U) Creditors had very few comments on the first draft of the annual report prepared by the Secretariat. The IMF said it strongly supported the initiative. The UK suggested -- and the Secretariat agreed -- that it would be helpful to include a section describing how the resources made available by debt relief are used to reduce poverty. The Secretariat seeks proposed edits within two weeks and aims to finalize the draft report by the beginning of May.

STAPLETON